

Private Letter Ruling: The statute of limitations on refund claims does not preclude a taxpayer from claiming an increased foreign tax credit as an offset against a deficiency arising from a federal change, even if the statute of limitations has expired for filing a claim for refund based on the increased credit.

February 5, 2003

Dear:

This is in response to your letter dated November 29 2002 to Paul Caselton, in which you request a Private Letter Ruling (**PLR**) on behalf of COMPANY1. Review of your request for a **PLR** disclosed that all information described in paragraphs 1 through 8 of subsection (b) of 86 Ill. Adm. Code Section 1200.110 appears to be contained in your request. The **PLR** will bind the Department only with respect to COMPANY1 for the issue or issues presented in this ruling. Issuance of this **PLR** is conditioned upon the understanding that neither COMPANY1 nor a related taxpayer is currently under audit nor involved in litigation concerning the issues that are the subject of this ruling request.

The pertinent parts of your letter, including facts and analysis as you have presented them are as follows:

As discussed, and on behalf of the above-referenced entity (the “partnership”), we respectfully request a private letter ruling granting permission to file one amended return per year (1996, 1997, and 1998) for each resident partner rather than multiple amended returns reflecting changes resulting from (1) several completed multi-year partnership audits by states where nonresident returns are filed; (2) several ongoing multi-year partnership audits by states where nonresident returns are filed; and (3) an ongoing multi-year partnership federal audit that will conclude after the completion of the state audits. This private letter ruling is based on the facts set forth below.

#### Facts

The partnership and its affiliated companies operated in various states through May 7, 1999 and had partners who were Illinois residents. On May 7, 1999, the partnership was terminated and succeeded by the COMPANY2, which continued the operations in various states. The partnership is currently under multi-year audit by the Internal Revenue Service (“IRS”) for the tax years 1996 through 1998 and several states for the tax years 1996 through 1999. The state audits are expected to conclude prior to the IRS audit. In addition, the partnership has completed several state audits for the aforementioned period. All state audits have resulted or will result in additional tax being paid each year by the Illinois resident partners to nonresident states. This will result in potential refunds in Illinois each year based on the availability of additional credits for taxes paid to nonresident states. The IRS audit will likely result in assessments that will also increase the taxes paid each year to the nonresident states, also resulting in potential refunds in Illinois based on the availability of additional credits for taxes paid to nonresident states. Notwithstanding, the IRS audit will likely result in assessments in Illinois that exceed the total potential refunds available each year attributable to additional credits for taxes paid to nonresident states.

Due to the multiple ongoing federal and state audits, as well as the completed state audits, multiple amended returns are required for each year for each resident partner to report the federal changes to Illinois and claim all additional credits for taxes paid to nonresident

states. Moreover, by the time the IRS concludes, the statute of limitations for additional credits for taxes paid to nonresident states will have expired in some or all instances. When this occurs, the Illinois resident partners will be barred from reporting the correct amount of credit for taxes paid to other states on the amended Illinois return that reports the federal audit changes.

### Issue

Can one amended Illinois return be filed per year (1996, 1997, and 1998) for each resident partner once the IRS audit concludes that (1) reports the federal changes, and (2) reflects all additional credit claims for taxes paid to nonresident states for (a) the state audits finalized prior to the conclusion of the IRS audit, and (b) the increased taxes paid to nonresident states resulting from the IRS audit adjustments, regardless of whether the statute of limitations has expired for any of the additional credit claims?

### Discussion

35 ILCS 5, Section 911(a) provides, in pertinent part, that a claim for refund shall generally be filed not later than three years after the date the return was filed or one year after the date the tax was paid, whichever is later. In cases involving notification of a change to a federal income tax return, 35 ILCS 5, Section 911(b)(1) provides that a claim for refund may be filed within two years after the date on which such notification was due (regardless of whether such notice was given). 35 ILCS 5, Section 506(b) requires notification to occur within 120 days of the alteration of the federal income tax return. As amended in 1989, this section deleted references to income tax returns of any other states. 35 ILCS 5, Section 601(b)(3) permits resident taxpayers to claim a credit against Illinois income tax for income tax paid to other states for a tax year on income which is also subject to the Illinois income tax.

Ordinarily, when a partnership is audited by a state and assessed additional tax, each partner can claim a credit in the resident state for taxes paid to a nonresident state, so long as the statute of limitations for doing so is open in the resident state. This process can become administratively burdensome when a partnership with numerous partners is audited by multiple states. This is because for each individual state audit, an amended return is required for each partner to claim in the state of residence the additional credit for taxes paid to nonresident states.

This matter is further complicated when a partnership is also audited by the IRS. If the IRS partnership audit results in assessments that also increase the taxes paid to the states, each partner again can claim a credit in the resident state for taxes paid to the nonresident states, so long as the statute of limitations for doing so is open in the resident state. This produces yet another wave of amended returns for resident partners to claim in the state of residence the additional credits for taxes paid to nonresident states.

In addition, in instances (such as this one) where an IRS audit concludes after (1) the completion of the state audits, and (2) the statute of limitations for claiming additional credits for taxes paid to nonresident states has expired, the resident partners are precluded from claiming the proper credit for taxes paid to nonresident states on the Illinois amended

return that reports the federal audit changes. This preclusion denies the resident partners any meaningful opportunity to obtain the benefits of such credits. In order to remedy this inequity, permission is requested by the partnership to file one amended Illinois return per year for each nonresident partner once the IRS audit concludes that (1) reports the federal changes, and (2) reflects all additional credit claims for taxes paid to nonresident states for (a) the state audits finalized prior to the conclusion of the IRS audit, and (b) the increased taxes paid to nonresident states resulting from the IRS audit adjustments, regardless of whether the statute of limitations has expired for any of the additional credit claims. By granting permission to do so, the resident partners will be able to report the correct amount of credit for taxes paid to nonresident states on the amended Illinois return that reports the federal audit changes.

Furthermore, permission as requested above should be granted in order to alleviate the heavy administrative burden on the partnership and the Illinois Department of Revenue with regard to the filing of multiple amended returns for each resident partner. By permitting one amended Illinois return each year for each resident partner once the IRS audit concludes, reflecting the results of all nonresident state audits (whether or not time barred) and the federal audit, efforts of both the partnership and Illinois will be streamlined with respect to the preparation, review and processing of the amended returns.

Based on the foregoing, the partnership respectfully requests permission to file one amended Illinois return for each resident partner once the IRS audit concludes that (1) reports the federal changes, and (2) reflects all additional credit claims for taxes paid to nonresident states for (a) the state audits finalized prior to the conclusion of the IRS audit, and (b) the increased taxes paid to nonresident states resulting from the IRS audit adjustments, regardless of whether the statute of limitations has expired for any of the additional credit claims.

Enclosed please find a properly executed Illinois power of attorney (Form IL-2848) authorizing us to represent the partnership in connection with this matter.

#### DEPARTMENT RULING

Please be advised that the Department is amenable to granting the relief requested in your correspondence. You correctly point out that the filing of amended returns on behalf of each resident partner as a consequence of the state and federal audits at issue will be cumbersome and constitute an administrative burden. You also raise a valid point that the statute of limitations for each resident partner to file refund claims based on increases in the credit for taxes paid to other states will likely expire before the IRS audit will be completed in this matter. However, the long-standing policy of the Department has been that nothing in the statutes of limitations for filing refund claims prohibits the correction of any erroneous item on a return for a tax year or the filing of an amended return to make such a correction after the limitations period for that year has expired. In such a case, while the taxpayer filing the amended return will not receive the benefit of a refund, the Department will recognize the corrected amount of tax/or credit for purposes of computing the correct amount of any underpayment.

Also, there is no statutory provision requiring the filing of any notice of a decrease in Illinois income tax liability resulting from an increased credit for taxes paid to another state. Therefore, the

Department hereby grants permission to COMPANY1, and its Illinois resident partners to file one amended return per year (for 1996, 1997, and 1998) for each Illinois-resident partner rather than multiple amended returns reflecting changes resulting from (1) several completed multi-year partnership audits by states where nonresident returns are filed; (2) several ongoing multi-year partnership audits by states where nonresident returns are filed; and (3) an ongoing multi-year partnership federal audit that will conclude after the completion of the state audits, provided that the reports of the changes resulting from the federal audits are timely filed and that the increased foreign tax credit claims are used only to offset the deficiency that would otherwise result from the federal changes, unless a claim for refund based on such credits would otherwise be timely.

The facts upon which this **PLR** are based are subject to review by the Department during the course of any audit, investigation or hearing and this ruling shall bind the Department only if the material facts as recited in this ruling are correct and complete. This ruling will cease to bind the Department if there is a pertinent change in statutory law, case law, rules or in the material facts recited in this ruling.

Sincerely yours,

Jackson E. Donley,  
Senior Counsel-Income Tax